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Decision 05-09-018 September 8, 2005

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Application of Southern California Edison  
Company (U 338 E) for Approval of Economic  
Development Rates.

Application 04-04-008  
(Filed April 5, 2004)

Application of Pacific Gas and Electric Company  
to Modify the Experimental Economic  
Development Rate (Schedule ED). (U 39 E)

Application 04-06-018  
(Filed June 14, 2004)

(See ATTACHMENT B for Appearance List)

**ALTERNATE OPINION OF COMMISSIONER KENNEDY ACCEPTING  
ECONOMIC DEVELOPMENT RATE TARIFFS**

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## **OPINION ACCEPTING ECONOMIC DEVELOPMENT RATE TARIFFS**

### **I. Summary**

The economic development tariffs proposed in these two applications were designed to attract business to California, to expand business in California, or to retain business in California. On August 30, 2004, these two applications were consolidated in the Scoping Memo and Ruling of Assigned Commissioner. Hearings were held on October 18, 19, 20 and 21. This decision accepts the proposed economic development rates (EDR), as modified herein, on the ground that the utilities have demonstrated that the proposed rates have the potential to accomplish the established goals of attracting business to the state, and/or expanding or retaining business in the state. Furthermore, the utilities have proposed effective measures for preventing free-ridership by ineligible businesses, and, therefore, have ensured that the proposed EDR will be beneficial to ratepayers.

#### **A. Southern California Edison (SCE)**

In Application (A.) 04-04-008, SCE requests authority to offer three types of EDR agreements: (1) the EDR-Attraction; (2) the EDR – Expansion; and (3) the EDR - Retention. Each EDR agreement would provide participating customers a discount from the customer’s otherwise applicable tariff (OAT) beginning at 25%, and declining by 5% each year over a five-year term. SCE proposes to make these options available to customers whose demands exceed 200 kilowatts (kW), provided the customer could demonstrate to SCE’s satisfaction that “but-for” the incentive provided by the EDR agreement, the customer would not retain

its load in SCE's service territory, or would not otherwise locate or expand its load in California.

SCE requests authority to make these options available to eligible customers until December 31, 2006, and to assess whether their availability should be extended beyond that date in Phase 2 of SCE's 2006 General Rate Case (GRC). The underlying premise of its application is the need to promote economic development in its service territory by offering an incentive to customers who would otherwise not retain or locate their load in California. SCE contends that this would benefit its ratepayers in a number of ways, including the reduction of rates by spreading SCE's and the Department of Water Resources (DWR) fixed costs over a larger base of retained sales.

SCE believes that its proposal ensures that participating customers will provide benefits to other ratepayers by producing a positive contribution to margin (CTM)<sup>1</sup> over the term of the EDR agreements. Under its proposal, the amount of the discount for bundled-service customers would be calculated based on their total bill on their OAT.<sup>2</sup> For ratemaking purposes, SCE would first apply revenue received from EDR customers to make a full contribution to nonbypassable charges

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<sup>1</sup> Contribution to margin (CTM) is the difference between the average rate paid by a customer and the marginal cost of serving that customer. (D.96-08-025, p. 5.)

<sup>2</sup> The total bill for bundled-service customers includes all delivery charges (Transmission, Distribution, DWR Bond Charge, Public Purpose Program, and Nuclear decommissioning Charge) as well as SCE's generation charge and the charge for DWR power. For DA customers, the bill includes all delivery charges and the DA cost responsibility surcharge (CRS), but no SCE generation or DWR power charges. (SCE/Jazayeri; Ex. 1:16.)

and the DWR power charge, and then apply the remaining revenue to distribution and generation charges.

For direct-access (DA) customers, SCE initially proposed to calculate the discount using the same percentage reduction it applies to the bills of bundled-service customers; however, since DA customers do not purchase generation service from SCE or DWR power, the amount of their discount would be smaller. SCE would once again first apply revenue received from DA customers to nonbypassable charges, excluding the DWR bond charge, with the remaining revenue applied to SCE's delivery charges and to the CRS paid by DA customers.<sup>3</sup>

In order to provide an incentive for customers to remain on the EDR agreement, thereby ensuring that ratepayers receive the expected benefits over the term of the EDR agreement, SCE proposes a liquidated damage provision. The liquidated damages would recover the discount provided to EDR customers whose agreements were terminated prematurely, unless termination was due to shut down of the facility. SCE's proposal also includes measures intended to prevent the use of these agreements by free-riders, *i.e.*, those customers that would have retained or located the load in California in any event without receiving the discount provided by the EDR agreement.

#### **B. Pacific Gas and Electric Company (PG&E)**

In A.04-06-008, PG&E proposes enhancements to its existing Schedule ED rate:

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<sup>3</sup> The amount of revenue apportioned to the CRS would be allocated in accordance with D.03-07-030, *i.e.*, to the DWR Bond Charge, Historical Procurement Charge, Competition Transition Charge, and DWR Power Charge.

- Expand the availability of the rate option to PG&E's entire electric service territory;
- Increase the percentage and length of time over which non-generation tariff rates would be adjusted;
- Expand the eligibility to include business retention in addition to business attraction and expansion, and include the State in making the determination as to which businesses qualify for the rate;
- Remove the caps on the number of possible customer participants and amount of load; and
- Remove the disincentive to PG&E's application of the rate in the form of shareholder financial participation.

(Exhibit 7, PG&E Direct Testimony, p. 1-1.) PG&E's original proposal has been modified over the course of the proceeding to incorporate the following elements:

- A liquidated damages clause applicable to customers who sign an enhanced ED contract based on fraud or misrepresentation. (Exhibit 9, PG&E Rebuttal Testimony, p. 1-15.) For such instances, PG&E is willing to support liquidated damages that would require the customer to pay twice the difference between the otherwise applicable tariff (OAT) and the amounts paid by the customer under the enhanced Schedule ED rate. (Exhibit 29, Joint Proposal, p. 1.)
- Affirmation that bundled service customers on the Schedule ED rate should be able to opt for procurement service from another provider (*e.g.*, direct access or community choice aggregation), assuming the customer is otherwise eligible for such service. (Exhibit 9, PG&E Rebuttal Testimony, p. 1-7.)

- Clarification that PG&E would not use the enhanced Schedule ED in combination with PG&E's Distribution Bypass Deferral Rate (*i.e.*, Schedule E-31). (Exhibit 9, PG&E Rebuttal Testimony, p. 1-6.)

### C. Joint Utility Proposal

At the request of the presiding Administrative Law Judge (ALJ), a Joint Proposal was developed by Edison and PG&E, with each utility compromising on various aspects of its independent proposals. The ALJ had commented that if he were to recommend that the Commission authorize SCE and PG&E to offer the EDRs, that whatever proposal he recommended would apply equally to both utilities, *i.e.*, the terms of the agreements would be consistent, that he would include a liquidated damage provision in his recommendation, and that the agreement could only be offered to a customer whose relocation choice was outside California. Pursuant to the ALJ's request, SCE and PG&E submitted a common proposal that eliminates all prior differences between SCE and PG&E in terms of their respective EDR proposals. The Joint Proposal (Exhibit 29) provides the following:

Issue	Joint Proposal
Eligibility Test	"But-for" test, as proposed by SCE and described in Exhibit 2, p. 3.
Sunset Date	December 31, 2009.
Program Cap	100 MW as proposed by SCE, clarifying that the cap would apply at any point in time for active contracts, based on contract demand.
Liquidated Damages	For misrepresentation or fraud, liquidated damages equal to 200% of the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT.  For other cases of early termination (excepting business closure or reduction of load without

Issue	Joint Proposal
	relocation), liquidated damages equal to the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT less 15%, plus interest on that difference at the 90-day commercial paper rate. (The OAT less 15% figure was chosen because it reflects the average incentive expected over the life of the contract.)
Form of Affidavit	Separate from contract as proposed by PG&E, except that it would be modified to reflect the “but for” test and would include the following statement: “On an annual basis, the cost of electricity for [Company Name] at this facility represents approximately [Number] % of operating costs.”
3 <sup>rd</sup> Party Review	Office of California Business Investment Services (CalBIS) to perform preliminary review, with the utility performing final review and determination. Approval by CalBIS is “necessary but not sufficient” for eligibility.
Eligible Customers	All customers above 200 kW, except state and local government and residential customers. Offer of rate at utility discretion.
Calculation of Incentives for Bundled Customers	Incentive calculated on total OAT and, for ratemaking purposes, reflected in the utility-retained generation and distribution revenues only.
Calculation of Incentives for Direct Access (DA) Customers	Equivalent incentive for DA customers, based on using bundled-service customer’s generation cost as a proxy.
Floor Pricing and Marginal Costs	Limit the discount to ensure revenue does not fall below floor price, which consists of transmission charges, public purpose program (PPP) charges, nuclear decommissioning (ND) charges, DWR Bond charges, Competition Transition Charge (CTC), marginal costs for distribution, and, if a bundled-service customer, marginal costs for generation. Floor price to be based on customer-specific marginal costs, up to the OAT. Unit marginal costs to be established at beginning of customer contract.
Shareholder Contributions	None



SCE and PG&E recommend that the Commission adopt the provisions of the Joint Proposal as a comprehensive package that would apply to both SCE and PG&E, without shareholder financial participation.

**D. Position of Other Parties**

The Alliance for Retail Energy Markets and the Western Power Trading Forum (AReM/WPTF) state that the Joint Proposal “offers a compromise that is worthy of serious consideration by the Commission,” that AReM/WPTF support the Joint Proposal, and that the Commission should adopt it “as a reasonable means of resolving the issues extant in this proceeding.”<sup>4</sup>

Modesto Irrigation District (Modesto ID) supports the Joint Proposal provided that the Commission imposes shareholder participation in the discount, precludes the discounting of nonbypassable charges, and prohibits the combination of the EDR agreements with other similar discounts.<sup>5</sup> Merced Irrigation District (Merced ID) reluctantly supports the Joint Proposal with a proposed modification to the language and form of the customer affidavit, and a proposal for a third-party reviewer of eligibility other than CalBIS.

The Office of Ratepayer Advocates (ORA) supports a slightly-modified version of SCE’s position prior to the Joint Proposal with 25% shareholder participation in the funding of the discount.<sup>6</sup> Aglet

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<sup>4</sup> AReM/WPTF OB, pp. 3, 4, 6.

<sup>5</sup> Modesto OB, p. 1.

<sup>6</sup> ORA OB, p. 1.

opposes EDR, but states that if the Commission approves the applications, it should modify the Joint Proposal to impose further restrictions.<sup>7</sup>

## **II. The Need for Economic Development Rates**

SCE and PG&E assert that California's business climate is one of the most unfriendly in the nation, with the cost of doing business the fourth highest in the nation. At the same time, California's regulatory environment is one of the most burdensome in the nation. Utility costs in California exceed the national average, and exceed the average utility costs in the western states which directly compete with California for businesses and jobs. All these negative factors have contributed to the migration of jobs and economic activity from California to other states. Utility costs are playing a more important role in attracting business to other states. Some states' economic development agencies specifically target California businesses.

While California's economy, on a stand-alone basis, is currently rated as the fifth or sixth largest in the world, the California Business Roundtable (CBRT) reports that "California's regulatory environment is the most costly, complex, and uncertain in the nation."<sup>8</sup> Worker productivity, venture capital funding, higher education facilities and California's concentration of science and technology give California distinct advantages over many locations. However, California is often overlooked when it comes to a company's decision to relocate or to expand. A major factor is the cost of doing business. Other western states

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<sup>7</sup> Aglet OB, pp. iv, 2.

<sup>8</sup> CBRT, Bain & Company California Competitiveness Project, 2/25/04 Exec. Summary, p. 5. (Exh. 6.)

are becoming the preferred locations for businesses to expand and establish new facilities due to their lower costs and fewer regulatory burdens.

Various studies maintain that the cost of electricity is one of the main contributors to the cost of doing business in California. It has been suggested that electric rates alone cause one sixth of an estimated 30% cost premium for doing business in California.<sup>9</sup> Economic development corporations outside California highlight California's higher electricity costs as one of the major reasons to move into their states. In the NCBER study, the "cost of occupancy and utilities "in Los Angeles County is identified as the third-highest factor cited in relocation decisions.<sup>10</sup> Utility costs, as a factor contributing to business relocation decisions, are only exceeded by the overall costs of doing business and insufficient room for expansion.<sup>11</sup>

The Milken Institute notes that other states are aggressively attempting to lure manufacturers away from California by highlighting their lower business costs, particularly electricity and tax rates.<sup>12</sup> By comparison, California's electricity rates are exceptionally high. At the time the Milken Institute report was released, California had electricity costs that were double the national average and were the highest rates in

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<sup>9</sup> CBRT, Bain & Company California Competitiveness project, 2/5/04 Exec Summary, p. 3. (Exh. 6.)

<sup>10</sup> L.A. Region NCBER Final Report, December 2003, p. 38. (Exh. 1.)

<sup>11</sup> *Ibid.*

<sup>12</sup> Milken Institute, Manufacturing Matters, August 2002, p. 6. (Exh. 7.)

the contiguous United States.<sup>13</sup> Rates have since been reduced from their high point during the energy crisis, but for rates in effect as of July 1, 2003, SCE had the fourth highest commercial electric rate and eighth highest industrial rate of 166 investor-owned electric utilities included in the analysis.

Section 740.4(h) of the Pub. Util. Code requires the Commission to allow recovery through rates of expenses and rate discounts supporting economic development programs to the extent that ratepayers “derive a benefit from those programs.” SCE and PG&E believe that ED rates will benefit utility ratepayers in two ways.

First, the utilities state that successful economic development projects benefit ratepayers directly by increasing the revenues available to contribute to the utilities’ fixed costs of doing business, thus lowering rates to other customers. The ability to offer a rate that is lower than the tariff rate, but higher than marginal costs, helps to maintain or attract CTM for the benefit of ratepayers to the extent that the customers would not otherwise remain or locate within the utilities’ service territory absent the incentive. If the customer chooses a location outside of the utilities’ service territory, its CTM is zero, thus depriving other ratepayers of the positive CTM that would have been made available from the rate offering.

Second, the utilities contend that in addition to direct benefits to other ratepayers, economic attraction and retention activities also provide indirect benefits to ratepayers in the form of increased employment opportunities and improved overall local and economic vitality. Local

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<sup>13</sup> Milken Institute, *Manufacturing Matters*, August 2002, p. 39. (Exh. 7.)

communities benefit from the economic multiplier effect resulting from local spending by newly employed, or continuously employed, workers where the businesses locate. One of the indirect results from the strengthened economic base is the fuller use of the utilities' transmission and distribution facilities which further reduce rates.

The adoption of this EDR should also be viewed as a stopgap measure to address a small part of the harmful impacts the current rate levels have on California's economy and the state's potential for economic growth and development. In fact, we believe that the EDR program will work to lower rates, albeit slightly, by allowing fixed and sunk costs to be spread out over a larger customer base. However, the need for this EDR serves as a flashing warning light that we must continue to take all steps necessary to address the level of rates in California.

ORA, in evaluating the need for ED rates, questions whether a different type of program might be more effective in meeting the goals of retaining businesses in California or whether different classes of customers, such as small businesses, are more in need of an ED rate. ORA questions whether such a program will foster the overall goal of improving the California economy and increasing jobs in California. It contends that while parties cite a variety of formal studies and informal opinions to support their own position, either for or against ED rates, in the end the need for such programs appears to be subjective. ORA has concluded, however, that while all the questions about the need for ED rates cannot be answered in the affirmative with absolute confidence, such a program could bring benefits to ratepayers, but only if such a program contains safeguards to prevent free-riders by being carefully targeted at

businesses which are at risk of leaving the State or not locating in California.

Merced ID argues that it is not clear that the utilities have met their burden of proof that any of their ED rate proposals should be adopted. However, it says that if we adopt an ED rate program we should not tilt the competitive playing field in favor of the utilities nor shift costs to other ratepayers. Merced ID's traditional district boundaries are entirely encompassed within PG&E's service territory. As a result, Merced ID and PG&E compete head-to-head for customers. Merced ID asserts that PG&E's proposed ED rate could result in tilting the competitive playing field in PG&E's favor, in unqualified customers using the ED rate, and in cost-shifting under the ED rate at a relatively high level given the depth of the discounts offered. Merced ID contends that factors other than energy drive business location decisions.

### **III. Discussion**

Section 740.4(h) of the Pub. Util. Code requires the Commission to allow recovery through rates of expenses and rate discounts supporting economic development programs to the extent that ratepayers "derive a benefit from those programs." As the utilities have demonstrated, the implementation of successful economic development projects would benefit ratepayers directly by increasing the revenues available to contribute to the utilities' fixed costs of doing business, thus lowering rates to other customers. The ability to offer a rate that is lower than the tariff rate, but higher than marginal costs, helps to maintain or attract CTM for the benefit of ratepayers to the extent that the customers would not otherwise remain or locate within the utilities' service territory absent the incentive. If the customer chooses a location outside of the utilities' service

territory, its CTM is zero, thus depriving other ratepayers of the positive CTM that would have been made available from the rate offering.<sup>14</sup>

In addition to direct benefits to other ratepayers, economic attraction and retention activities also provide indirect benefits to ratepayers in the form of increased employment opportunities and improved overall local and economic vitality. Local communities benefit from the economic multiplier effect resulting from local spending by newly employed, or continuously employed, workers where the businesses locate. One of the indirect results from the strengthened economic base is the fuller use of the utilities' transmission and distribution facilities which further reduce rates.<sup>15</sup>

As indicated above, the derived benefits from a successfully implemented EDR program appear to sufficiently satisfy the ratepayer benefit test. Despite these apparent ratepayer benefits, Aglet contends that one of the utilities' primary measurements of ratepayer benefits—the Ratepayer Impact Measure (RIM) test—could be adversely impacted by even a relatively low level of free-ridership. The utilities argue, however, that the “free-rider” rate would have to be as high as 75% for the enhanced EDR program not to benefit ratepayers.<sup>16</sup> As the utilities have demonstrated, past experience with the existing Schedule ED, in conjunction with the additional eligibility limitations proposed for the

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<sup>14</sup> Exhibit 7, PG&E Direct Testimony, Chapter 6; PG&E Rebuttal Testimony, Chapter 3.

<sup>15</sup> *Ibid.*

<sup>16</sup> Reply Brief of Pacific Gas and Electric Company, December 15, 2004, p. 19.

enhanced EDR program, indicates that the actual level of free-ridership would be substantially below the 75% break even level.<sup>17</sup> It is reasonable to assume, therefore, that Aglet's concerns of relatively low levels of free-ridership adversely impacting ratepayer benefits are unfounded. Past experience dictates that although the EDR system will inherently attract a small number of free-riders, these aberrations will be insufficient to offset the widespread ratepayer benefits that the incentives will entail.

To ensure that free-ridership does not approach this 75% threshold, however, the utilities have proposed a number of preventative measures. First, they propose requiring potential applicants to provide a signed affidavit stating that:

1. But for receipt of the discounted development rate and the terms of the Agreement, either on its own, or in combination with an economic development incentive package, the Applicant's load would not have been located, added, or retained within California;
2. The load to which the Agreement applies represents kilowatt-hours (kWh) that either (i) do not already exist in the State of California, or (ii) the Applicant considered relocating to a location outside of the State of California;
3. Applicant has discussed with the Company the cost-effective conservation and load management

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<sup>17</sup> *Ibid* p. 19.



measures the Applicant may take to reduce their electric bills and the load they place on the Utility System. (See Attachment A).

4. On an annual basis, the cost of electricity for [Company Name] at this facility represents approximately [Number] percent of operating costs.

The affidavit serves to address two key concerns expressed by several of the parties. First, it requires the applicant, under penalty of law, to assert that were it not for the Agreement (on its own or in combination with an economic development incentive package), it would have failed to expand, relocate or add its load in the State of California. Next, it addresses the legitimate concern of expanding demand on an already overburdened utility system.

Furthermore, by requiring the applicant to discuss the cost-effective conservation and load management measures it could take to reduce its impact on the utility system, the utilities are making a concerted effort to comply with the Commission's goals of conservation and demand side management. Although a simple "discussion" between the applicant and the utility may not be enough to ensure that any of the available conservation measures are actually pursued, it does demonstrate a desire on behalf of the utilities to keep potential EDR participants apprised of the Commission's conservation goals and methods for meeting these objectives.

Although we believe that the utilities should make every conceivable effort to persuade EDR customers to meet the Commission's identified conservation and efficiency objectives, we recognize that a majority of EDR applicants may be seeking relief from high energy rates

because they are facing difficult financial constraints. These constraints may limit an applicant's ability to focus on the Commission's goals of energy efficiency and demand side reduction. For this reason, we will not order the utilities to require new EDR applicants to assume the necessary costs of participating in structured energy efficiency or conservation programs. Rather, in an effort to guarantee that "discussions" with EDR applicants do not become mere formalities, we direct the utilities to perform an energy audit for all applicants, during which they must present to these applicants all cost effective energy efficiency and demand side management programs that have a five year or less pay-back period.

Additionally, in an effort to ensure that applicants are not tempted to falsify their affidavits and thereby engage in free-ridership, the utilities have advocated for the imposition of liquidated damages in cases of misrepresentation or fraud. These liquidated damages will be equal to 200% of the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT.

For cases of early termination (excepting business closure or reduction of load without relocation), liquidated damages equal to the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT less 15%, plus interest on that difference at the 90-day commercial paper rate.

The proposed liquidated damages penalties are severe. In most cases, the types of businesses applying for EDR exemption will be those operating on thin margins or facing difficult cost constraints. The prospect of incurring damages equal to 200% of the cumulative differences between their normal bills and their bills under the EDR, a sum that could equal

hundreds of thousands of dollars, will undoubtedly provide a moment of pause for any applicant considering engaging in either fraud or misrepresentation. The same can be said of the proposed penalties for early termination. Although these penalties are not as severe as those for fraud or misrepresentation, they will almost certainly act as a deterrent to any applicant contemplating abusing the EDR system for short-term gains.

As a final measure for limiting free-ridership, the joint utility proposal calls for CalBIS<sup>18</sup> to perform a preliminary review of applicants, but leaves it to the utility to perform the final review and determination. CalBIS approval will be necessary but not sufficient for eligibility. Merced ID opposes this portion of the joint utility proposal. It argues that CalBIS is not truly an independent arbiter; its job is to provide reasons for a business to stay or locate in California. It also states that the utilities have failed to develop with CalBIS the procedure to be used for verification. Further, Merced ID argues, the utilities will not be independent decision-makers.

In this instance, as an entity whose traditional district boundaries are entirely encompassed within PG&E's service territory, and thereby competes directly with the utility for customers, it is evident why Merced ID might attempt to discredit the third-party review process. Despite Merced ID's concerns, it is clear that CalBIS has the expertise and staff to

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<sup>18</sup> California Business Investment Services, or CalBIS, is the lead State government office responsible for helping domestic and foreign corporations make direct investments in California. CalBIS works to expand, attract and retain business in California.

identify and screen legitimate economic development candidates, and its position as the state's preeminent evaluator of economic development issues gives it unique and early access to would-be EDR applicants. Additionally, because coordination with the utilities is already within the scope of its work, CalBIS would not require payment for its services.

However, Merced ID's concerns regarding CalBIS's role as an independent third party reviewer are not entirely unfounded. As it pointed out, CalBIS's primary function is the attraction of business to California and the expansion of business within our borders. For this reason, CalBIS may be limited in its ability to provide a wholly unbiased analysis of EDR applicants. Hence, the third party review will be conducted by CalBIS staff under the supervision of The California Business, Transportation and Highway Agency (BTH), or their designee. The synergy between these two institutions will ensure that the third party reviewer will make appropriate recommendations of EDR applicants and will act as both a cost-effective and vigilant deterrent to free-ridership.

In evaluating the role of EDR in a business expansion setting, it is instructive to consider the experience of one potential recipient of PG&E's proposed ED rate. On August 13, 2004, in this proceeding, PG&E filed a motion to provide interim rate relief to a customer, Amy's Kitchen, considering expansion and relocation outside of California. Amy's Kitchen has its corporate headquarters in Santa Rosa, as well as all of its production facilities. It employs 700 people and makes 120 products that generate annual revenues of approximately \$100 million. Amy's Kitchen moved into its current 107,000 square foot facility in 1995. There is no room left in which to expand. Now the company needs approximately 80,000 more square feet of production space to keep up with projected

demand for its products. Amy's Kitchen, at the time of the motion, was considering different siting alternatives: (i) expand new operations out-of-state while maintaining existing operations in Santa Rosa; (ii) move existing operations out-of-state and expand operations at that consolidated out-of-state location; and (iii) keep existing operations in Santa Rosa and expand operations there as well. The cost of electricity in the out-of-state proposals has been as low as 4 cents/kwh.

Amy's Kitchen uses approximately 8,400 MWh annually and receives electric service under PG&E's E-19S rate schedule. In 2003, Amy's Kitchen paid approximately \$1.2 million in electricity charges. If PG&E's 2003 GRC Phase II rate design proposal (A.04-06-024) is adopted, with an approximate 10% rate reduction for the schedule serving Amy's Kitchen, PG&E estimated that Amy's Kitchen would pay about \$927,000 per year for electricity. Factoring in a 25% EDR reduction would reduce Amy's Kitchen's first year electric bill by approximately \$232,000, to \$695,000.

On November 30, 2004, PG&E filed its request to withdraw its motion for an interim decision for Amy's Kitchen, stating that Amy's Kitchen had decided to locate its expansion project in Oregon, keeping its existing facilities in California. PG&E's request to withdraw its motion was granted on December 15, 2004.

Amy's Kitchen's decision to expand its business out of state, rather than at its headquarters in Santa Rosa, indicates the need for the Commission to develop a uniform structure for the application of EDR. In PG&E's August 13, 2004 Motion for an Interim Decision to apply the enhanced Schedule EDR to Amy's Kitchen, the utility indicated that the company needed to make a decision on its expansion project by November 2004. When the Commission had not made a decision on the motion by

November, Amy's Kitchen executives were forced to decide on its expansion without the opportunity to consider reduced electricity rates.

Although it is not clear whether the failure to attain a timely Commission decision on the application of EDR was *the* decisive factor in Amy's Kitchen's decision to expand out of state, it is evident that company executives were forced to make a crucial evaluation without factoring EDR savings into their calculation. The fact that the Commission's current policy of evaluating EDR applications on a case-by-case basis may have been responsible for a prominent California business locating a major expansion out of state is reprehensible, and illustrative of the shortcomings of the current regime. By giving utilities the discretion to extend EDR to qualified candidates, the Commission will be taking an important step toward ensuring that energy rates no longer act as a hindrance to companies looking to do business in California.

Finally, the Commission feels compelled to address the issues of reporting regulations and compliance standards in regard to the utilities' proposed EDR programs. While we feel it important to give the utilities the latitude to offer admission to the EDR program as they see fit, we also recognize the significance of maintaining the Commission's oversight role in this matter. For this reason, starting in 2006 and stretching until the program's sunset date in 2009, we will ask the utilities to provide the Commission with an annual compliance report detailing all EDR applicants, the contents of the CalBIS and BTH review for these applicants, and the utilities final selection of EDR candidates. Additionally, in an effort to ensure that the utilities do not use the revised rates as a competitive tool, we will require SCE and PG&E to inform all applicants of

the appeal and complaint avenues available at the CPUC to those who believe they were unfairly denied admission to the EDR program.

As a final safeguard against the utilities using the EDR rates as a competitive tool, SCE and PG&E will be required to submit a brief report to the Secretary of BTH, or the Secretary's designee, each time an applicant is rejected against the Secretary's recommendation. This report must recount with specificity why the utility decided as they did. Following a review of these materials, at the Secretary's discretion, BTH will be able to file a complaint with the Commission if she believes the applicant has been unfairly rejected. If the applicant and BTH prevail in the proceeding, the utility will be required to cover the costs incurred by these parties through their participation in the case. If the Commission deems the applicant eligible for the rate, the rate will be made available, retroactive to the date the complaint was filed. The purpose of this reporting requirement is to ensure that qualified applicants are not turned away for arbitrary reasons, such as their preference for DA as opposed to bundled service. In the end, we believe this compliance filing will help ensure that the EDR program is functioning in a fashion that is attracting, expanding and retaining business in California, and preventing the type of free-ridership and competitive behavior that may undermine these goals.

The Joint Proposal went a long way to further the goals that an economic development rate can achieve (business retention, attraction and development), yet we believe that the Joint Proposal unnecessarily favored bundled customers over Direct Access or even potential Community Choice Aggregation customers by limited the components of their bills to which the discount would be applicable. PG&E highlights this situation appropriately in its comments on the alternate of Commissioner Kennedy:



In the context of the Kennedy Alternate, it would be remiss of PG&E not to acknowledge here that a large industrial transmission-level direct access customer in PG&E's service area has recently expressed concerns that, while the customer looks forward to considering an ED rate as part of a package of incentives, the ED rate incentives in the joint proposal would not provide it sufficient inducement to expand and refurbish its existing facility in California. This is because the level of incentives that the customer might expect to get under the joint proposal would be significantly limited by the floor price, which consists of the transmission rate and certain non-bypassable charges.<sup>19</sup>

We agree with PG&E's observation and appreciate the fact they brought this situation to our attention. By compiling more charges into the price floor, the Joint Proposal would have made the ED rate more attractive for a bundled customer than for a direct access customer whose rates are not bundled. This scenario could have set up the situation in which a direct access customer, in order to obtain the ED rate, might move back to bundled service. The ED rate would not be customer-neutral, but more importantly, might not accomplish the goals of promoting business retention, attraction and development because some classes of customers will not even consider this incentive package due to its inability to provide a discount that could influence their business decision. We therefore modify the Joint Proposal to exclude certain charges from the price floor.

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<sup>19</sup> PG&E Initial Comments, p. 3, August 15, 2005.

This decision accepts an amended version of the utilities' Joint Proposal, as outlined below:<sup>20</sup>

<b>Issue</b>	<b>Amended Proposal</b>
Eligibility Test	"But-for" test, as proposed by SCE and described in Exhibit 2, p. 3.
Sunset Date	December 31, 2009.
Program Cap	100 MW as proposed by SCE, clarifying that the cap would apply at any point in time for active contracts, based on contract demand.
Liquidated Damages	For misrepresentation or fraud, liquidated damages equal to 200% of the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT. For other cases of early termination (excepting business closure or reduction of load without relocation), liquidated damages equal to the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT less 15%, plus interest on that difference at the 90-day commercial paper rate. (The OAT less 15% figure was chosen because it reflects the average incentive expected over the life of the contract.)
Form of Affidavit	Separate from contract as proposed by PG&E, except that it would be modified to reflect the "but for" test and would include the following statement: "On an annual basis, the cost of electricity for [Company Name] at this facility represents approximately [Number] % of operating costs."
3 <sup>rd</sup> Party Review	Office of California Business Investment Services (CalBIS) to perform preliminary review <u>under supervision of the California Business</u> .

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<sup>20</sup> The Amended Proposal is almost identical to the Joint Proposal of the utilities except that some language has been stricken from and added to the Joint Proposal. The stricken language has been left in the tables but has a line through it while the added language has been underlined.

Issue	Amended Proposal
	<u>Transportation and Highway Agency (BTH)</u> , with the utility performing final review and determination. Approval by CalBIS is “necessary but not sufficient” for eligibility.
Eligible Customers	All customers above 200 kW, except state and local government and residential customers. Offer of rate at utility discretion.
Calculation of Incentives for Bundled Customers	Incentive calculated on total OAT <del>and, for ratemaking purposes, reflected in the utility retained generation and distribution revenues only.</del>
Calculation of Incentives for <u>Community Choice Aggregation (CCA)</u> and Direct Access (DA) Customers	Equivalent incentive for DA <u>and CCA</u> customers, based on using bundled-service customer’s generation cost as a proxy.
Floor Pricing and Marginal Costs	Limit the discount to ensure revenue does not fall below floor price, which consists of <del>transmission charges, public purpose program (PPP) charges, nuclear decommissioning (ND) charges, DWR Bond charges, Competition Transition Charge (CTC),</del> marginal costs for <u>transmission</u> , distribution, and, if a bundled-service customer, marginal costs for generation. Floor price to be based on customer-specific marginal costs, up to the OAT. Unit marginal costs to be established at beginning of customer contract.
Shareholder Contributions	None

Additionally, in an effort to reach the goal of promoting economic development on a statewide basis, we will also strongly encourage San Diego Gas and Electric (SDG&E) to file applications that are consistent with the spirit of the EDR programs approved for PG&E and SCE. In keeping with the goals of the EDR programs adopted herein, their proposal should promote business retention, attraction and development. We believe that by requiring SDG&E to participate in the EDR process we will ensure that qualified applicants in the San Diego area do not miss out on the benefits proffered to those in the PG&E and SCE service areas.

#### **IV. Comments on Proposed Decision**

The proposed alternate decision of the Commissioner in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. Initial comments were filed on August 15, 2005, and reply comments were filed on August 19, 2005. Changes to the decision based upon comments have been made herein.

#### **V. Assignment of Proposed Decision**

Susan P. Kennedy is the Assigned Commissioner and Robert Barnett is the assigned ALJ in these proceedings.

#### **Findings of Fact**

1. The cost of electricity is one of the major contributors to the cost of doing business in California. By some estimates electric rates cause about one sixth of what some experts believe is the overall 30% cost premium for doing business in California.
2. The implementation of successful economic development projects would benefit ratepayers directly by increasing the revenues available to contribute to the utilities' fixed costs of doing business, thus lowering rates to other customers.
3. In addition to direct benefits to other ratepayers, economic attraction and retention activities also provide indirect benefits to ratepayers in the form of increased employment opportunities and improved overall local and economic vitality.
4. For the enhanced ED program not to benefit ratepayers instances of free-ridership would have to be as high as 75%.
5. The utilities' past experience with the existing Schedule ED, in conjunction with the additional eligibility limitations proposed for the enhanced EDR,

indicates that the actual level of free-ridership would be substantially below the 75% break even level.

6. The utilities' have proposed measures, including a mandatory affidavit, the imposition of liquidated damages for fraud, misrepresentation and early termination, and a third-party review by CalBIS and BTH, that will effectively curb the frequency of potential free-riders.

7. Amy's Kitchen, a company that could expect to receive a GRC electric rate decrease plus a further EDR decrease of 25%, opted to locate its expansion facilities in Oregon because the Commission failed to issue a timely decision on the matter.

8. The experience of Amy's Kitchen demonstrates that the current EDR regime must be overhauled to allow the utilities the discretion to offer these rates to qualified applicants and, therefore, accomplish the goals of retaining business in the state, attracting business to the state, and encouraging California businesses to engage in in-state expansion.

9. An EDR that applies differently based upon a customer's classification (i.e., direct access versus bundled) does not meet the Commission goals of promoting business retention, attraction and development because one group of customers may see more benefit in the incentive package over the other group.

### **Conclusions of Law**

1. Rate reductions to attract or retain business are in accord with the legislative precept to "encourage economic development." (Pub. Util. Code § 740.4.)

2. The rate reductions and procedures requested by the applicants and as modified herein have been justified. (Pub. Util. Code § 454(a).)

## **O R D E R**

1. The modified requests for economic development rates in Applications (A.) 04-04-008 and 04-06-018 are approved.
2. Beginning in 2006, and on an annual basis thereafter until the program's 2009 sunset, PG&E and SCE are ordered to submit to the Commission a compliance filing listing all EDR applicants, the contents of the CalBIS review for these applicants, and the utilities final selection of EDR candidates.
3. San Diego Gas and Electric is strongly encouraged to file applications that are consistent with the spirit of PG&E and SCE's electric economic development rate programs as adopted herein. Their proposal should promote the goals of business retention, attraction and development.
4. SCE and PG&E shall file tariffs consistent with the adoption of the EDR programs as adopted herein within 15 days of the effective date of this decision, and agreements as they are entered into. These tariffs shall be effective subject to confirmation of compliance by the Energy Division.
5. Application 04-04-008 and A.04-06-018 are closed.

This order is effective today.

Dated September 8, 2005, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
GEOFFREY F. BROWN  
SUSAN P. KENNEDY  
DIAN M. GRUENEICH  
JOHN A. BOHN  
Commissioners

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**Attachment A**

**AFFIDAVIT FOR ECONOMIC DEVELOPMENT INCENTIVE RATE**

By signing this affidavit, an Applicant who locates, adds, or retains load in the service territory of [utility name] hereby certifies and declares under penalty of perjury under the laws of the State of California that the statements in the following paragraphs are true and correct.

1. But for receipt of the discounted economic development rate and the terms of the Agreement, either on its own, or in combination with an economic development incentive package, the Applicant's load would not have been located, added, or retained within California.

2. The load to which the Agreement applies represents kilowatt-hours (kWh) that either (i) do not already exist in the State of California, or (ii) the Applicant considered relocating to a location outside of the State of California.

3. Applicant has discussed with the Company the cost-effective conservation and load management measures the Applicant may take to reduce their electric bills and the load they place on the Utility System.

4. On an annual basis, the cost of electricity for [Company Name] at this facility represents approximately [Number] percent of operating costs.

**(End of Attachment A)**



**ATTACHMENT B**

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(END OF ATTACHMENT B)

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